What the experts do with their 1/3 lump-sum payment

When you retire and your RA (Retirement Annuity) matures, you can withdraw a maximum of 1/3 of it as a lump sum. We asked an expert what options you have with this lump-sum amount to secure your finances into retirement.

Does my RA actually mature?

A common misconception is that your RA ‘matures’ when you turn 55, but this isn’t strictly the case, as Werner Vlok, Business Development Manager at Glacier by Sanlam, explains: “An RA does not have a maximum retirement age, so you are not forced to retire from your RA. You can keep it until the day you decide to retire after the age of 55. You can even keep it after you’ve formally retired from your job. You don’t ever have to retire from an RA if you don’t want to.”

Naturally, there are benefits to leaving your RA to grow until you retire at, say, age 65. “It’s best to keep that saved as long as possible for the capital to grow, to supply you with an income for when you decide to retire,” adds Werner.

The rule of thirds

RAs are governed by the Pension Funds Act, and because you can enjoy tax breaks on your contributions, there are rules the RA adheres to. The rule most applicable when retiring from the RA is that you aren’t allowed to withdraw more than 1/3 of the total amount as a cash lump-sum.

For example, if your RA’s total balance stands at R3 million, the maximum you’re allowed to withdraw any time after age 55 is R1 million (1/3). The remaining R2 000 000 (2/3) needs to be reinvested into a retirement income product.

What to do with your 1/3 withdrawal

You could choose to reinvest the entire sum of your RA into a retirement income product, but Werner notes that there are also advantages from a tax-savings perspective (depending on your marginal tax rate in retirement) to look at other options for where to invest your first R500 000 taxfree portion, or at least some of it. “If you invest this portion in a discretionary investment, such as a unit trust investment plan, for example, although you’ll be liable for capital gains tax when selling units, you won’t pay income tax on any money withdrawn from this investment,” he explains. “However, you will pay income tax on the income drawn from a retirement income product such as an annuity.

“You’ll be exposed to market movements in a unit trust investment, whereas the portion in the retirement income product (if you’ve selected a life annuity) is protected from market volatility. So there are choices to be made which is why we always advocate getting proper advice. A qualified adviser will look at your overall financial, as well as your tax, position and help structure your portfolio accordingly.”

At Glacier, retirees have the option to buy a life annuity as a voluntary purchase – in other words, take your 1/3 and buy a life annuity product with it. “This is designed with risk-averse clients in mind, and is also a tax-friendly option,” says Werner.

Options for your 2/3 reinvestment

The remaining 2/3 of your RA cannot stay in the RA and needs to be reinvested to secure your long-term income for retirement. This means there’s less flexibility than you would enjoy on your discretionary 1/3 withdrawal. You cannot touch this money, no matter your age, except for when you draw down your regular monthly income. “One usually plans for a term of 30 years,” says Werner. “Together with your financial adviser you’ll need to decide on a retirement income product – these are mostly living annuities or life annuities. A combination of these products is also a very attractive option as each product has its own strengths and weaknesses and combining them should give you a better outcome over your retirement journey.”

With these, your drawdowns will be subject to tax according to the marginal tax table. “You get taxed on your monthly income as if it’s a salary,” says Werner.

Is there a middle ground?

“It’s good to have money both in retirement income products, as well as in non-retirement products,” shares Werner. Drawing from both of these means the tax burden of your retirement income product isn’t felt as harshly on your finances.

“Say, for instance, you’ve invested R2 million in a living annuity, and you start drawing an income of R20 000,” suggests Werner. “That puts you in a specific tax bracket (a 26% marginal tax bracket).” If you lower your drawdown rate to as little as R12 000 and supplement that with non-taxable drawdowns from your discretionary investment, you draw less from your annuity, saving you tax:

Living annuity drawdowns	Discretionary investment drawdowns

	Taxed at 26%	Taxed at 0%
Scenario 1	R20 000	R0
Scenario 2	R12 000	R8 000

Deciding what to do can be quite complex and, therefore, we always advocate to *talk to a qualified financial adviser* to assist you with these decisions," he says. Learn more about flexible retirement solutions here.

Please consult with a financial adviser before you take any action regarding your savings and investments.

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